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MEMORANDUM FOR: Mr. Sidney J. Zabludoff
Council on International
Economic Policy

SUBJECT : Contribution to CIEP
Annual Report

1. Attached is the draft chapter requested on economic planning in the major industrial countries for the President's Annual International Economic Report.

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2. If you have any questions, please call [redacted]

Attachment: As Stated

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ECONOMIC PLANNING IN MAJOR INDUSTRIAL COUNTRIES

OVERVIEW

Comprehensive multiyear economic planning is conducted on an indicative basis in France, Italy, and Japan, among the major industrial nations. Plans serve as guidelines for decisionmakers in both private and government sectors. Although the highest government authorities may formally approve completed plans, their endorsement does not commit them to take the steps needed to translate projections into reality. In some cases, governments lack the constitutional power needed to force decisionmakers in the private sector to cooperate in carrying out approved plan goals.

Planning is relatively sophisticated in France, where a large number of economic decisionmakers in the government and private sectors help formulate plans in great detail. The French government is highly centralized, and its top echelon has potent tools for influencing lower-level decisions. These tools are not fully utilized, however.

At the other extreme, comprehensive planning does not exist in Canada, West Germany, or the United Kingdom. In Canada, an advisory body of non-government technicians and spokesmen for various groups merely suggests economic goals. In West Germany and the United Kingdom, the closest thing to comprehensive planning is a continuing effort to project government expenditures five years in advance.

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There is no apparent correlation between the degree of multiyear, comprehensive economic planning and a country's economic success. Planning is believed to have smoothed French economic progress by illuminating potential bottlenecks and, perhaps, by stabilizing investment. But, a number of planned targets have not been achieved, and successes are attributed mainly to factors other than planning. West Germany has registered a good economic performance without comprehensive planning, and Japan has done well with a planning system that is more formal than operational.

Planning is not the principal instrument of government economic influence in any of the major industrial countries. In all of them, governments make economic decisions continuously on the basis of changing conditions and judgments. All of the governments use conventional tools of monetary and fiscal policy to promote real growth, contain inflation, and influence the balance of payments. The nationalized sectors of Italy, the United Kingdom, and France are big enough to exert a sizable influence on growth through their investment patterns and other activities. Government influence on the economy is probably the greatest in Japan, where government and business traditionally cooperate closely and make important decisions on a consensus basis.

FRANCE

Economic planning in France was introduced in the aftermath of World War II, but its roots go back much further. For centuries, the central government played an important role in controlling economic matters, thus preventing the spirit of free enterprise from developing as fully as it did elsewhere. The economic difficulties of the 1930s -- worse in France than in most other countries -- culminated in the nationalization of several key industries. Given this background, there was little disagreement among French leaders at the end of the war that national planning was needed not only to rebuild the economy but also to restore France's former greatness. The need for planning in order to utilize Marshall Plan aid effectively reinforced this conclusion.

The French plans are indicative, not compulsory. They establish guidelines that are not binding on participants -- even when these are government agencies or government-owned corporations. Focusing primarily on the industrial sector of the economy, the plans typically cover a five-year period. The Sixth Plan, for example, covers the years 1971 through 1975.

French planners explicitly recognize the advantages of the market mechanism and seek to complement it rather than supplant it. The main goals are to make sure that decision-making in both the public and private sectors is done in a coordinated fashion. Emphasis is placed on making the plan as democratic as possible by giving all interested parties a chance to be heard during the planning process.

While the broad objectives of the planning process have remained unchanged, the plan itself has expanded considerably in scope over the years. The First Plan (1946-1952) focused on making up for war damage and concentrated heavily on six basic industries. The scope of later plans was broadened to include all industrial sectors, some regional planning, and some social concerns -- such as income distribution. The Fifth Plan (1966-1970) gave high priority to encouraging firms to increase their size through merger or expansion. Emphasis in the current plan is on improving industry's ability to meet foreign competition.

Formulation of the French plan begins with the president making the basic choices that establish the framework and main goals of the plan. The Commissariat General du Plan then prepares an outline of the plan in accordance with these directives and sends the results to parliament for further discussion. Following debate

by various interest groups and parliament, numerous planning commissions work out detailed plans for specific sectors and fit these sectoral plans together into a consistent whole. Further discussion follows, with the final plan ultimately being approved by parliament.

Targets are set for the final year of the plan period, not for each intervening year. Initially an estimate of gross domestic product and its main components is made for the final year. Using input-output tables, the planners then determine the corresponding demand for intermediate goods and ultimately calculate the amount of new labor and investment needed. These preliminary targets go to the individual planning commissions, where representatives of business, government, and labor work out the detailed sectoral estimates.

Compliance with plan targets is not compulsory. Neither parliament nor private businesses nor government corporations are compelled to adhere to the plan in their decisionmaking. It is hoped, however, that because these groups all helped formulate the plan, they will accept it and act accordingly. The government has broad powers to encourage the private sector to act appropriately, including control of private bond issues and licensing of construction projects. In practice, however, the

government has never made full use of its powers, perhaps fearing that this would create a too-authoritarian image.

Judgments on the success of French planning are mixed, with foreign observers generally being more critical than the French. Industrial production growth targets set by the planners have generally been met or exceeded. It is likely, however, that similar growth would have been achieved without planning. France has had the benefit of many positive factors since the war, including US aid, good natural resources, and large reserves of underemployed labor in agriculture. The rapid economic growth elsewhere in Europe has also provided a major stimulus. Perhaps most important, France's entry into the Common Market exposed French businessmen to the hot breath of competition for the first time, and they responded well. Planning probably helped to forestall bottlenecks and reduce fluctuations in investment, thus making the growth process smoother than it might have been.

While overall growth targets have generally been attained, the same is not true for more specific goals. There have been very large discrepancies in meeting targets for specific sectors, with some industries greatly over-fulfilling their goals and others falling short. Moreover, the economy has not been very successful in achieving targets set for the balance of payments and inflation.

ITALY

National economic planning has met with little success in Italy since its introduction with the Vanoni plan (1954-64) and formalization with the first Development Plan in the mid-1960s. Indicative in nature, planning is intended to afford a framework within which to formulate and conduct economic policy. It has concentrated on achieving full employment and accomplishing certain development objectives. Although the activities of Italy's extensive public sector have been somewhat influenced by economic planning, the technical rather than operational character of the planning has lessened its effectiveness. Indedd, the gap between plan objectives and results has been wide.

The failure of economic planning stems partly from built-in bureaucratic inefficiencies. Long delays between budget appropriations and expenditures frequently blunt planning efforts. Occasionally the assumptions underlying Italy's plans are unrealistic; for instance, a 4% annual price increase was assumed for the 1973-77 period in Italy's most recent draft plan.

Even more important, the advisory status of the planning body at the Ministry of the Budget and Economic Planning has contributed to unsuccessful plan implementation. Italy's planners do not participate in

the decision-making machinery of government and have no power to implement their ideas. As a result, their guidelines are often ignored not only by private companies but also by parliament and by public enterprises.

The projections for the first development plan (1966-70) were conceived as targets, but significant achievement proved impossible in the face of administrative delay. The plan itself was not enacted until a third of the period covered had already elapsed. A more flexible strategy was adopted in subsequent planning attempts, which have been essentially assessments of potential growth that are revised periodically. The avowed, if unfulfilled, goals of economic planning in Italy remain:

- achievement of the highest possible employment level;
- reduction in the per-capita income gap between northern and southern Italy;
- increased social investment, particularly in low-income housing;
- and, a general improvement in social services.

Considerable emphasis is put on bridging the income gap between the industrialized North and the less developed South. Per capita income in the South nevertheless remains only about half that in the North. To help achieve a more equal regional income distribution, parliament in 1971 empowered the Fund for the South (Cassa per il Mezzogiorno)

to commit well over $12 billion for investment in the South through 1975. In addition, governmental departments are supposed to make 40% of their investment in the South and state-controlled enterprises 60% of their industrial investments.

The most recent development plan draft foresaw an annual GNP growth rate of 6% in 1973-77 as the minimum needed to achieve sizable gains in employment and more efficient use of industrial capacity. Employment in industry and services was expected to expand by 1.3 million, while employment in agriculture was expected to decline by 700,000. The planners expected the current account surplus to decline to a low level by 1977.

Events, however, rapidly overtook this planning attempt. Because of an unanticipated sharp rise in world commodity prices, which coincided with a strong surge in domestic demand, Italy's trade account deteriorated much more rapidly than expected by the country's planners and domestic prices took off. Economic policy had to be redirected from growth to austerity to reduce the trade gap and dampen inflation.

The government has also dabbled in sectoral planning. Government agricultural policy through two Green plans in the 1960s facilitated improvements in

agriculture. In the early 1970s, the government attempted a national chemical plan that set investment guides for the industry. This plan foundered because of tensions between Italy's public and semi-public chemical giants. More recently, the government approved a national petroleum plan. This latest effort aims at guaranteeing a secure supply of crude oil through the ~~eventual establishment~~ of an annual supply plan and rationalization of the national refinery, transport, and distribution networks.

While the gap between planning goals and achievements has been great, the government still has considerable influence over economic development, mostly through traditional monetary policies, consultations with management and labor ,and the activities of state-controlled enterprises. Until recently the government rarely used fiscal policy as a demand management tool.

The public sector is particularly large in Italy, and the government is engaged in numerous banking and industrial activities. Over one-quarter of Italy's largest firms are state-owned or -controlled. State firms loosely work toward the aims of Italy's planners, combining the profit motive with social goals. They play an important countercyclical role, increasing expenditures during recessions and easing up on investment during booms. During the 1970-73 recession, when private investment

plummeted, increased public enterprise spending boosted the public share of fixed industrial investment to about one-half of total investment from its more usual one-third.

JAPAN

The Japanese government plays a key role in the economy. It uses many means, including formal economic planning, direct financial assistance, consultation and persuasion, monetary and fiscal policy, and foreign economic policy to influence economic development. Of these, medium-term plans and their implementation have probably had the least direct influence. Nevertheless, the extremely close, traditional relationship between the Japanese government and the business community has made many of the general themes and directions outlined in these plans achievable.

Tokyo has various policy planning tools at its disposal. The most general are the medium-term plans, usually for five years, formulated by the government's Economic Planning Agency. The plans are comprehensive and relatively specific, but their postwar record generally shows that they were not designed to generate the rapid growth actually realized and even failed to anticipate it. All the plans since the first for FY 1948-52 (the Japanese fiscal year runs through March of the following year) have had to be scrapped or revised, usually in about the middle of the plan period, when they became

obsolete. The FY1967-71 plan, for example, had achieved its goal for real growth by FY 1969.

The most recent plan to be implemented was the FY1970-75 Economic and Social Development Plan. As in the previous program, the stress was placed on controlling inflation and improving social infrastructure and the general well being of the population. For the first time, the planned rate of growth -- 10.6% -- was more in line with past experience. The average growth rate was only 8% during the first four years of the plan, however, and, given the current economic slowdown, will likely fall to below 6% for the plan period as a whole. Inflation, on the other hand, was seriously underestimated.

Another medium-term plan, this one covering the remainder of the decade, is currently under discussion in government and business circles. Drafted last year, the plan has been overtaken by domestic and international economic events. Given current and more pressing economic problems, longer-term planning is presently not considered of much utility or interest.

Monetary policy is the principal tool used by the government in influencing economic developments. The most potent weapon in this regard is "window guidance",

whereby an informal ceiling is placed on credits extended by individual banks. The use of fiscal policy as a countercyclical tool is relatively new. Until the mid-1960s, the government's goal was to have its budget play essentially a neutral role in the economy, avoiding excessive stimulation to an already rapidly growing economy and keeping government expenditures to a fairly constant share of GNP. In recent years, the government has assumed an active role in combating business slowdowns.

The major factor in the government's relatively successful promotion of economic growth is the close relationship between government and business. This relationship, termed "consensus management," is a distinctive feature of Japanese business life. It is based on economic and cultural patterns dating back at least over the past century and operates mostly in a traditional rather than legal framework.

Few major decisions are made by either government or business without extensive consultations with -- and usually consent from -- the other. Government ministries concerned with economic affairs maintain some 300 consulting committees for this purpose. This largely informal arrangement makes the decision-making process tedious and time-consuming, but when the consensus is reached, policy implementation is rapid and cooperation is generally assured.

Favorable cultural attitudes toward teamwork, the similar social and educational backgrounds of business and government leaders, the continued "retirement" of senior government officials to executive positions in industry, and the broad acceptance of key national economic goals combine to produce this continuing dialogue between the public and private sectors. Economic decisionmaking by consensus is, however, now undergoing its most severe test. In 1974, real output for the year is down for the first time since the war and inflation is its worst in 25 years. The policy dilemmas faced by the government in trying to solve or at least mitigate both problems have strained the long-standing cooperation among business, government, and labor.

UNITED KINGDOM

Comprehensive economic planning in the United Kingdom has been indicative in nature and none too successful. In the immediate post-World War II period, the Labor government endorsed a plan that consisted of goals for all the major economic variables, including gross national product, industrial production, employment, and prices. Measures needed to achieve these goals were not adopted, however, and the plan was quietly abandoned.

By the late 1950s, sentiment favoring a new attempt at comprehensive planning had grown. The United Kingdom had experienced recurring balance-of-payments crises, prices were rising rapidly, and investment had been interrupted repeatedly by measures aimed at solving balance-of-payments problems. In 1961, the National Economic Development Council (NEDC) was established to recommend policies to stimulate economic expansion. The planning function was vested in the Department of Economic Affairs, which in 1965 published a national plan incorporating most of the goals endorsed by NEDC, including a 4% annual increase in output and the curbing of consumption in favor of investment. Again the measures required to implement the plan were not adopted and the plan was abandoned.

-- At present, the cabinet retains final responsibility for the broad lines of economic policy. Programs and policies for coping with problems, such as inflation and labor disputes, are developed and implemented by the main government departments having economic responsibilities -- mainly the Treasury, the Department of Trade and Industry, and the Bank of England. In 1970, a Central Policy Review Staff was established within the Cabinet Office to work on the formulation and review of economic strategy. The NEDC still functions as an important advisory body on policy and is supplemented by more specialized advisory bodies.

The government budget is a long-range policy instrument even though it is continually used as a short-term economic stabilization tool. Expenditures are projected five years ahead, based on social requirements, as determined by appropriate government agencies and on projected resource availabilities.

Investment by nationalized industry plays a large role in British public finance, and the management of state industry has been the major element in British attempts to cope with lagging economic growth. However, most observers judge that nationalization has made little

difference in the coordination of British industry. Each nationalized industry is operated as a single unit, but the activities of the various industries are only loosely coordinated.

The Labor Government now proposes extending nationalization to the oil, shipbuilding, and aircraft sectors and establishing a new partnership arrangement between government and industry in an effort to foster economic growth. Under the partnership arrangement, a National Enterprise Board would be empowered to start new ventures, to extend public ownership into profitable manufacturing enterprises, and to provide government assistance to companies in short-term financial or commercial difficulties. A system of planning agreements between the government and major companies in key sectors would cover investment, pricing, productivity, employment and industrial relations, product development, foreign trade, and the interests of consumers.

WEST GERMANY

National planning in West Germany is essentially an extension of the budgetary process. It is used largely as a tool for analyzing and coordinating fiscal policy. Government planners do not set production or investment targets for any specific segments of the private sector, but the impact of proposed fiscal actions is considered. On a short-term basis, the government uses orthodox instruments of fiscal and monetary policy to encourage growth, combat inflation, and maintain a favorable balance of payments.

The budgetary plan covers a 5-year period. Revisions are made annually when the coming year's budget is prepared. The plan is a quantification of the broad economic goals of the government. The budget for the ensuing year requires legislative approval, however, and the plan in its entirety is intended as a guideline for parliamentary deliberation.

The West German government recently submitted the 1974-78 budgetary plan to the Bundestag. It provides for growth in federal spending slightly slower than the nominal GNP growth expected during the period. Nonetheless, certain elements of government expenditures will grow much faster

than GNP. Social welfare spending will receive the strongest emphasis, and foreign aid will also take a big jump. Outlays for defense and transportation are expected to grow much slower than total federal spending. The plan also highlights the prospects for larger federal deficits and the likely need for the government to compete increasingly for funds in the capital market.

Aggregate federal spending plans were initiated in 1967 following the enactment of the "Law for Promoting Stability and Growth." The law was intended to assure a balance of revenues and expenditures at the federal level and empower the government to take actions to smooth out cyclical economic fluctuations. It required extending the budgetary plan 3 years beyond the coming fiscal year. The plan is drawn up in the Ministry of Finance on the basis of spending projections by the various departments and is rolled forward one year during each planning session.

Advocates claim that presenting the legislator with a 5-year budget plan forces him to consider the long-term implications of taxing and spending decisions. Detractors reply that even with the plan, long-run considerations become sidetracked by immediate concerns, and rapidly changing economic situations quickly relegate the plan to obsolescence. A more telling criticism is that the plan is focused on

the demand side of the economic equation and furthermore generally excludes foreign demand. Changes in foreign demand often have prevented expectations from being realized.

CANADA

Canada does not have a formal system of comprehensive economic planning. Uncoordinated economic planning on a functional basis is extensive, however, at all levels of government. Specialized regional development agencies, ad hoc government task forces, and royal commission also perform limited planning activities.

Although the planning process is fragmented, signs are emerging that Ottawa is giving increased attention to closer coordination of economic planning. This trend is evident in the more frequent use of federal-provincial conferences to reach common positions on vital national issues, such as energy policy and economic development in western Canada. Those Canadians favoring a federal planning agency envisage it developing a broad framework of economic goals and priorities that would reflect a national consensus. Public and private organizations would plan their activities within this framework.

The Economic Council of Canada is the closest thing to a national planning body that Canada currently has. Created by parliament in 1963, the council is an independent advisory body. It has no operational duties or authority

and no government representatives among its members. The council is staffed by professional economists and representatives drawn from most sectors of the economy. The council's chief functions are to define social and economic goals, recommend policies that would achieve these objectives, and anticipate future problems.

The definition of a set of medium-term economic performance targets has been among the most important features of the council's work in recent years. Published in 1972 for the years 1973-75, the targets are updated each year to extend over the following three-year period. They are intended as a guide for policymakers and do not represent economic goals that Ottawa has formally adopted. The following are several of the targets outlined by the council for 1973-75:

Target	Average Annual Change (Percent)
GNP	6.0
Consumer expenditures	5.5
Fixed capital investment	10.0
Exports of goods and services	6.0
Output per person employed	2.8
Total employment	3.1

The council also has recognized the need for closer economic policy coordination between federal and provincial government and private industry. It has been in the forefront of a drive to hold an annual national economic conference to assess medium-term prospects within the framework of the council's published goals. The first such conference, dedicated by Prime Minister Trudeau to "government by objectives," was held in December 1973. Its results were mixed. The conference suffered because labor delegates were not involved in much of the initial preparation of position papers. Nonetheless, a broad consensus was reached on the urgent need to establish industrial development priorities and a national energy policy and to achieve better coordination of the objectives of the public and private sectors.